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No. 202.

OCTOBER TERM, 1930.

IN THE

Supreme Court of the United States

ROBERT H. LUCAS, Commissioner of Internal Revenue,
Petitioner,

v.

SALLIE H. HENRY.

IN RE PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.

BRIEF FOR SALLIE H. HENRY, Respondent.

WM. CLARKE MASON,
Attorney for Respondent,
2107 FIDELITY-PHILADELPHIA TRUST BLDG.,
PHILADELPHIA, PA.

MORGAN, LEWIS & BOCKIUS,
Of Counsel,
2107 FIDELITY-PHILADELPHIA TRUST BLDG.,
PHILADELPHIA, PA.

LAW & SCHOOL PUB. PHILADELPHIA

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v.

Sallie H. Henry.

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STATEMENT OF FACTS.

The statement of facts in the petition for the Government, while substantially correct in so far as it goes, omits certain facts which are essential to give a clear picture of the transaction out of which the respondent's loss arose.

A full and more complete statement of the facts is to be found in the opinion of Judge Woolley, for the Circuit Court of Appeals (Record, p. 94), in the case of Samuel F. Houston No. 199, and therefore no restatement of them will be made here.

BRIEF FOR SALLIE H. HENRY, RESPONDENT.

The following argument is substantially identical with the argument for the Respondent in the companion case of Samuel F. Houston,—No. 199, and is repeated here merely for the convenience of the Court.

The question as presented by the Government in the brief in support of the petition for writ of certiorari in this case is stated as follows (p. 10):—

> "Was it incumbent upon the respondent to establish the March 1, 1913, value of her property right acquired prior to that date, to support a claim for a deductible loss on the disposition of such property in 1921?"

The draftsman of this statement of the question assumes in it that there was no proof by the respondent of a valuation of the subject matter of the loss, and justifies his assumption in the reasons for granting the writ (pp. 7 and 8), by asserting that "The respondent presented no evidence of the value of her right on March 1, 1913."

The Statement of "Specification of Errors to be Urged" appears to present to this Court, as a reason why the writ should be allowed, that the Court below failed "to hold that only those losses are deductible from gross income which are sustained after March 1, 1913," and thereby permitted the deduction of a loss which had been suffered by the respondent prior to that date. This reason has no foundation in the opinon and judgment of the learned Court below, because the Court expressly found that the loss deducted by the taxpayer was sustained after March 1, 1913, and in the year of 1921, in the return for the income of which the loss was claimed.

The respondent expects to establish to the satisfaction of this Court in the course of the argument hereafter made that the contentions presented on behalf of the Government in support of its petition are unfounded.

In the first instance, however, the respondent suggests

that a reading of the opinion of the Circuit Court of Appeals (Record, p. 94 of the Samuel F. Houston Case No. 199) will show that this case is not one of public interest because its peculiar and unusual facts limit the decision of it to these taxpayers only, and that the general conclusions reached by the learned Circuit Court of Appeals are not in conflict with the decisions of this Court, but are in full accord with them.

The Record in this case shows that the Commissioner made no finding that the loss sustained by the taxpayer was prior to March 1, 1913, but on the contrary, in disallowing the loss the Commissioner made the following statement (Petitioner's Exhibit No. 7—Record, p, 80):

> "With regard to the dissallowance of $176,840.28, you are advised that under the provisions of Revenue Act of 1921, no loss can be determined with respect to the transaction in question until the stock which was received as reimbursement is disposed of and the evidence is to the effect that the stock was still in your possession at the close of the year 1921."

The subsequent rulings of the Department and decisions by the courts made this reason for disallowance insufficient. The Commissioner, as the record shows, shifted his ground on the appeal to the Board of Tax Appeals and asserted other reasons there set forth, including the contention that no loss could be sustained on a value of the "Segal Matters" as of March 1, 1913.

At trial the Commissioner made no effort to establish a March 1, 1913, value at less than the original subscription of the respondent to the guaranty fund in 1906, but not relying upon this failure of the Commissioner to sustain what the respondent then believed to be the Commissioner's burden, the respondent undertook to meet the requirements of the situation in a manner subsequently declared by this Court to be the obligation imposed by the statutes.

In *Reinecke* v. *Spalding*, 280 U. S. 227, this Court said:

> "Under the statute it became necessary for respond-

ent to establish the fair market value of her interest in the mines on March 1, 1913, *or at least that such value was not below what she claimed it was.*"

The record shows that the Respondent clearly established by opinion evidence, which was the only evidence available in the absence of market values, that the value of the Segal assets (the subject matter of the loss claimed), as of March 1, 1913, *was at least a value not below that of original cost in 1906.*

It is to be remembered that the cost of the "Segal Matters" under consideration, as of 1906, is the aggregate of the Guaranty Fund subscribed to by the Respondent, and others, by which they acquired rights in distribution of, the proceeds of the "Segal Matters," under the terms and conditions of the agreements which form a part of the record.

It is the difference between the Respondent's original cost and the value of her portion of the assets received in liquidation in 1921 which constituted the loss claimed, and the evidence, to which reference will be made, establishes, by the opinion of those competent to judge the fact, that the "Segal Matters," on March 1, 1913, had an estimated value sufficient to return the original cost and a profit.

It was decided by the parties in interest in 1915, while the "Segal Matters" were still being administered by The Real Estate Trust Company for its own account and as trustee for the subscribers, that an interpretation of the original agreements should be obtained from John G. Johnson, Esq., of Philadelphia, who was counsel for George H. Earle, Receiver, and joint author with him of the plan of reorganization of The Real Estate Trust Company. The opinion of Mr. Johnson was asked for and was rendered under date of July 5th, 1915. (Petitioner's Exhibit 3—Rec., p. 60.)

Mr. Johnson held that the "Segal Matters" were subject to sole administration by The Real Estate Trust Company within its uncontrolled discretion, and that the subscribers to the Guaranty Fund were entitled only to the exercise of an honest administration of ordinary prudence and intelligence and without power to interfere with or direct the manner or time of liquidation.

He further held that when the amount of realization reached Three million dollars, from whatever source acquired, the right of the Trust Company to any additional payment ceased and the right of the subscribers attached, and thereafter all proceeds from the disposition of Segal assets became the property of the subscribers to the fund.

It is to be remembered that Mr. Johnson's opinion was given while the administration of the "Segal Matters" was continuing and speaks of the future when interpreting the rights of the parties to interest, as well as to a pro rata share in the proceeds realized from liquidation of principal assets.

The conclusion which he reached formed the basis for the subsequent agreement entered into between the parties, Mr. Johnson said (Petitioner's Exhibit No. 3, Rec., p. 65):

> "Interest is to be allowed in case of an excess sufficient in amount; but it is to be allowed only to the contributors upon the amount of their contributions.
>
> "In my judgment, therefore, the contributors are entitled to any excess in the realization of the 'Segal Matters' which will arise after there has been received from the 'Segal Items' by way of proceeds of sale, and income anterior to their conversion, the sum of $3,000,000."

Mr. Johnson also stated that in his opinion the power to administer by the Trust Company exclusively was not limited by any duty to consult with the subscribers or their representatives.

The evidence justifies the conclusion that in 1916, the year in which the Supplemental Agreement was made (Rec., p. 67), the Respondent and the other subscribers had a reasonable expectation of a return of their subscriptions made in 1906, with interest or profit from the "Guaranty Fund."

The Respondent's witness, Samuel F. Houston, gave the following as his opinion evidence in this connection (Rec., p. 86):—

"At the time the agreement of 1916 was entered into by me, I was of the opinion that if the Sugar Company was as successful as we anticipated and hoped, the much desired result that the Real Estate Trust Company would work out from the Segal assets a sum sufficient to return to the subscribers the amount of their contributions need not be a matter of very long time."

* * * * * * *

There is no reference to this evidence in the Petition or in the Brief for the Government.

The continuing value of the "Segal Matters" equal to the original subscriptions is established for this case not only by this oral testimony produced before the Board, but by the agreement of May 5, 1916, between The Real Estate Trust Company of Philadelphia and the subscribers through their Committee following the opinion of Mr. Johnson, (Petitioner's Exhibit, No. 3, Rec., p. 60), where the whole intent of the agreement between the Trust Company and the subscribers, of whom respondent was one, was to provide for a realization on their subscriptions.

The law does not require, and certainly a taxing law should not be construed to require, proof by mathematical certainty of fact inherently not susceptible of such proof. The equity of a taxpayer, which he by his own act is incapable of reducing to possession and which is dependent upon the uncontrolled administration of someone else, cannot be measured to the last dollar by any known scheme of accounting or the far-reaching theories and rules of the tax gatherer.

In the present case the Respondent in 1906 backed her confidence in the hope of success from her subscription by paying $200,000 into the guaranty fund. This justifiable expectation of profit continued up to and beyond March 1, 1913. There are no facts upon the record to show that as of March 1, 1913, there was not ample foundation for the realization of this expectation.

All that the Respondent was required to prove was that as of March 1, 1913, the rights of the Respondent in the "Segal Matters" had a value no less than the amount of the original investment in 1906. This was proved as fully as the unusual character of the transaction permits—and no evidence to the contrary was offered by the Commissioner.

The "Segal Matters" had in 1906 an *uncertain value*. This fact is stipulated in the record (p. 40). As of March 1, 1913, they had an equally *uncertain value* but not evidenced to be less than the subscriptions to the Guaranty Fund. The Respondent proved an actual loss of the difference between the subscription to the Guaranty Fund and the value of the securities received in distribution in the sum of $176,208. It would seem that Respondent has sufficiently complied with the mandate of the Statutes, as interpreted by this Court, to sustain the deduction of the loss as claimed.

In passing upon the contention of the Commissioner in the Circuit Court of Appeals upon this question, which is the sole question urged upon this Court, the lower Court disposed of it in the case of Samuel F. Houston which was made applicable to this case also, in language which it might be helpful to repeat here (Opinion, Woolley, Circuit Judge, Record pp. 99-101 of Houston Case No. 199):—

> "Finally, the Commissioner says—and this is the specific reason which the Board of Tax Appeals gave for approving his action—that the taxpayer has failed to prove, as he was bound to do, any loss subsequent to March 1, 1913 by failing to prove the value of the taxpayer's rights in the Segal matters on that date.
>
> "The petitioning taxpayer says that his loss was sustained in the taxable year 1920 as that was the year in which, for the first time, the loss could, in the circumstances of this case, be determined, and that it could be determined then only by finding the difference between the value of what was received and the cost of his rights in the Segal matters.

"The Commissioner's contention is based on the wording of like provisions in various revenue acts (here Section 202 (a) (1) of the Act of 1918) and on their judicial interpretation to the effect that the loss, if any, is the difference between what was ultimately received for the rights in 1920 and their cost in 1906, or their value on March 1, 1913, whichever was lower. Goodrich *v.* United States, 255 U. S. 727; Walsh *v.* Brewster, 255 U. S. 536; United States *v.* Flannery, 268 U. S. 98; McCaughn *v.* Ludington, 268 U. S. 106; Ayer *v.* Blair, 26 Fed. (2d) 547.

"The petitioner does not question the law of those cases which is in effect that a loss in an ordinary transaction relating to property owned outright by the taxpayer and entered into before March 1, 1913 is determined by adopting either the value as of that date or the cost at the earlier date, whichever is lower, as a basis, but he maintains that all those cases deal with property having a readily ascertainable value such as real estate, instruments evidencing debt and the like, which is different from ascertaining a loss under a right of the character here involved where the result of the venture could not be known until the Segal matters had been liquidated and where, therefore, the loss of a guarantor, or the value of his correlative right to reimbursement, is not ascertainable until the guaranty transaction is liquidated and where, until then, no ascertainable loss had occurred.

"To work out this aspect of the question it will be necessary to determine generally the interest of the contributors and particularly the petitioner's interest in the Segal matters. It is, because of their nature, difficult to give them a legal definition. Speaking of them in the singular number, it is certain that the petitioning contributor had no legal interest in the Segal securities or matters, or any legal claim to them. Legal title and the right fully to dispose of them was

exclusively in the Trust Company. The petitioner had, however, a right to a share of the residue of the proceeds of their liquidation, whether in cash or its equivalent. That right was in the nature of a chose in action yet a very restricted chose in action which he could not enforce until liquidation of the Segal matters had been fully completed, whenever that should be. The right, being a chose in action, was property. Being property, it was subject to disposition through testacy, intestacy and sale, which, so far as the record shows, did not occur in any instance. Being a right in property it had a value, potential at least, and a value, varying perhaps in mental contemplation, which persisted throughout the fourteen years it was held. Confessedly, it had, after the beginning and throughout that period, no market value for there were no sales. Nor did it, conceivably, have an ascertainable intrinsic value. Therefore it had no calculable tax value. The value of the right immediately after the beginning and to the very end depended on what the Trust Company had done with the Segal matters, what it was doing with them and what it would do with them in the future, and, finally, what in the future would be the outcome. To determine, in view of these variable factors, or lack of factors, its true or approximate value on a given date, as that of March 1, 1913 selected by the Commissioner as the basis of the tax calculation, was a sheer impossibility. The only fixed factors in the situation were those of cost in 1906 and return in 1920. It follows that the proper basis for measuring the petitioner's admitted loss—because the only possible basis—was that of cost and return. While by force of statute and judicial decisions March 1, 1913 is, in given instances, a critical date in computing income taxes, it is not in every instance a controlling date. If in this case the taxpayer had claimed a loss in 1913 on this transaction, he would, without doubt, have been met by the

Commissioner's ruling and the decision of the Board of Tax Appeals that he was anticipating a loss because the transaction was not closed; while on the other hand if the taxpayer had, after March 1, 1913, sold his right in the Segal matters at a figure which showed a profit over cost in 1906, though its value on March 1, 1913 could not be ascertained, the government would, we surmise, have exacted a tax on the profit. This is not an exaggerated illustration for if the recovery from the American Sugar Refining Company had been for the $10,000,000 demanded there would have been profits—indeed very large profits—coming to the contributors to the guaranty fund.

"We are constrained to hold that the petitioner suffered a deductible loss, that it was sustained by him in 1920 and that the amount of the loss was properly determined by him to be the difference between his subscription to the guaranty fund in 1906—cost—and the value of his pro-rata share of the proceeds of that fund when received by him in 1920."

The argument for the Government in the Circuit Court of Appeals presented several questions which have been abandoned in this petition, and no comment upon them is required other than to suggest that there appears to be no more merit in the sole question supported by the Government's brief than there was in those which were abandoned.

The opinion of the learned Circuit Court of Appeals clearly shows in the statement of facts how singular is the case of this respondent, and her associates as to whom the petitions have been filed, and how obvious the conclusion must be that the decision of these cases cannot be a precedent generally. This fact would seem sufficient to justify the denial of the petition for a writ of *certiorari*. U. S. *v.* Rimer, 220 U. S. 547; Furness, Withy & Co. *v.* Yang-Tsze Ins. Ass'n, 242 U. S. 430. The most casual reading, however, of the opinion of Judge Woolley, for

the Circuit Court of Appeals, shows how well founded, in passing upon these unusual facts, are his conclusions of law, and that they so fully accord, in principle, with all of the applicable decisions of this Court that there is no reason for a further hearing because the ultimate result would appear to be an affirmance of the judgment rendered below.

It is respectfully submitted that the petition for the writ of *certiorari* in the above entitled cause should be denied.

WM. CLARKE MASON,
Attorney for Respondent.
2107 Fidelity-Philadelphia Trust Building, Philadelphia, Pa.

MORGAN, LEWIS & BOCKIUS,
Of Counsel,
2107 Fidelity-Philadelphia Trust Building, Philadelphia, Pa.